
NIH Division of International Services

2004-2005

Income Tax Handbook

For

Visiting Foreign Scientists

At The

National Institutes of Health



U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES
PUBLIC HEALTH SERVICE
NATIONAL INSTITUTES OF HEALTH

The information provided in this handbook has been developed specifically for visiting scientists at the National Institutes of Health. It is not an official Internal Revenue Service (IRS) document and cannot be cited as a final authority. Information in this booklet has been compiled from the following IRS publications:

- Publication 519 – *U.S. Tax Guide for Aliens*
- Publication 901 – *U.S. Tax Treaties*
- Publication 463 – *Travel, Expenses Entertainment, Gift and Car Expenses*
- Publication 521 – *Moving Expenses*
- Publication 508 – *Tax Benefits for Work-Related Education*
- Form 1040 and Form 1040NR Instructions
- Form 8843 and Form 8843 Instructions

And the following state publications:

- 2004 Maryland Tax Handbook

The information provided is not all inclusive of the tax laws and regulations applicable to nonresident and resident alien taxpayers. The Internal Revenue Service and the State Comptroller should be contacted for official interpretations of income tax regulations.

Kathryn Bridges Tax Service, Inc.
Non-Immigrant Taxation Specialist
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WHERE TO GET FEDERAL AND STATE TAX FORMS, PUBLICATIONS AND INFORMATION

Federal

IRS toll-free numbers in the U.S. for various services are:

Recorded Tax and Refund Information	1-800-829-4477
Forms and Publication Orders	1-800-829-3676
Tax Information and Notice Inquiries	1-800-829-1040

Local IRS office locations:

- Bethesda, MD - 11510 Georgia Ave., Wheaton, MD; phone (202)283-8097
- Frederick, MD – 201 Thomas Johnson Dr., Frederick, MD; phone (301) 695-7615
- Baltimore, MD – 31 Hopkins Plaza, Baltimore, MD; phone (410) 962-7969

Forms and publications can be downloaded from the IRS's Internet Web Site at **www.irs.gov**

State

You can find general information and download forms and instructions from the following Internet web sites:

- Maryland – www.Marylandtaxes.com
- District of Columbia - www.cfo.dc.gov
- Virginia - www.tax.state.va.us
- North Carolina - www.dor.state.nc.us
- Arizona- www.revenue.state.az.us
- Montana – www.discoveringmontana.com/revenue

GENERAL INFORMATION

US Tax Facts

- The tax year is the calendar year (January 1 - December 31).
- There are specific tax rules that apply to foreign nationals. These rules are explained in detail in IRS Publication 519. If you are present in the U.S. with a “J” visa, you are required to file a tax form even if you have no income or all of your income is from a foreign source. In most cases, a state tax return form is also required.
- Tax forms to be used are Form 1040NR if you file as a nonresident alien or Form 1040 if you file as a resident alien. A “dual-status” taxpayer must file both Forms 1040 and 1040NR.
- Tax return forms are due on April 15th of each year, reporting income taxation for the previous calendar year.
- To claim exemption from U.S. income tax under a treaty agreement, you must meet certain requirements. Even if your entire income is excludable, you must still file the tax report at the end of the year and explain your treaty position.
- It is your responsibility to compute your own tax and determine whether you have a balance due or can expect a refund of overpaid taxes. You may hire a professional tax consultant or accountant to prepare your taxes.
- You may apply for a 4-month extension by filing federal Form 4868 by April 15. If you apply for an extension, you must still pay your tax by April 15. Form 4868 gives you additional time to fill out the forms.
- If you are due a refund, you will normally receive a check from the IRS in approximately 6-8 weeks after filing your tax return. You may receive your refund faster if you choose to have the check deposited electronically. If you have a balance due, you must include a check with your tax return at the time of filing.
- You are required by the IRS to have a social security number for proper identification of your tax returns, estimated tax declarations, etc., and to assure that you are properly credited with any tax withheld, estimated tax payments, or final tax payment. This number should be used on all tax return forms, payment vouchers, remittance checks, and correspondence with the IRS concerning your taxes.
- Additional penalties and interest are normally assessed if the return is not filed or if your tax is not paid by the due date.
- A copy of all tax reports filed should be retained in your permanent files for a minimum period of three years.

Definitions

Adjusted Gross Income (AGI) – Your total income reduced by certain adjustments.

Audit – An examination of your tax return by the Internal Revenue Service.

Credits – An amount that reduces your tax if you qualify for the credit.

Deductions – Deductions reduce your taxable income. There are two types of deductions:

- The **standard deduction** is a certain given amount that you are allowed to deduct based on your filing status. *Nonresident alien taxpayers, however, are not allowed to take the standard deduction.* Resident alien taxpayers must choose between itemizing deductions or claiming the standard amount.
- **Itemized deductions** are certain allowable individual expenses and are reported on Schedule A. *Nonresidents must itemize their deductions.*

Dual Resident Taxpayer – An individual who is both a tax resident of the U.S. according to the IRS substantial presence test and a tax resident of a foreign country under the resident article of the tax treaty.

Dual-Status Taxpayer – An individual who is both a resident alien and a nonresident alien in the same tax year.

Exemptions – A given amount that reduces your taxable income. Each person filing a tax return is allowed to claim his or her own personal exemption. The amount for 2004 is \$3,100. Resident taxpayers can also claim additional exemptions for qualifying dependents. *Nonresidents are generally not allowed to claim exemptions for dependents.*

Exempt Individual – A person who is present in the U.S. with an “F”, “J”, “M”, or “Q” visa. These individuals do not count days for the IRS substantial presence test when they first come to the U.S. An exempt individual is not someone who is tax exempt. It is someone who is exempt from counting days for purposes of the substantial presence test.

Filing Status – Your tax filing status is based on your marital status. There are five different filing status categories:

- **Single** – An individual who is not married.
- **Married filing separately** – A married individual reporting income separately from their spouse.
- **Married filing jointly** – Available only to married resident alien taxpayers; married resident aliens can file jointly even if only one spouse has income.
- **Head of household** – Generally applies to an unmarried individual with a qualified dependent such as a child.
- **Qualifying widower** – Applies to the first two years after the death of a spouse as long as the widow/widower does not remarry.

A nonresident is restricted to using either the “single” or “married filing separately” filing status (depending on legal marital status).

Grant – An allowance or award for study, research, or training. A grant is not considered to be compensation for personal services as long as there is no requirement for the individual to provide services to the organization.

Gross Income – The total amount of income that you receive *before* any subtractions for taxes, insurance or other items.

Income Tax – A tax assessed on income. U.S. citizens and residents are taxed on worldwide income. Nonresidents are taxed only on U.S. source income.

Internal Revenue Service – The government agency responsible for the assessment and collection of income taxes.

Nonresident Alien – Residency status for tax purposes. A nonresident alien does not have a green card or does not meet the IRS substantial presence test.

Resident Alien – Residency status for tax purposes. A resident alien will either have a green card or meet the IRS substantial presence test.

Social Security Number – Every U.S. citizen and anyone who works in the U.S. must have a social security number. This number is your identification number and account number with the IRS. You should include your SSN on all correspondence with the IRS.

Social Security Tax – A retirement tax based on income received for personal services. Employers are required to withhold social security taxes. The employee pays ½ of the tax and the employer pays the other ½. Services performed by a nonresident alien temporarily in the U.S. under subparagraph F, J, M, or Q of the Immigration and Nationality Act, as amended, are exempt from Social Security Tax for a period of 2 or 5 years. Non-service grants are not subject to Social Security Tax. J-2 visa holders with work permission are subject to social security taxes.

Substantial Presence Test – Determines residency status by counting the number of days you are present in the U.S. during each calendar year.

Tax Identification Number (ITIN) – If an individual needs a tax identification number for reporting purposes but is not eligible for a social security number, they can apply for an individual tax identification number. Every dependent claimed on a tax return must have either a social security number or tax identification number. Apply for an ITIN by filing Form W-7 with your Form 1040NR.

Taxable Income – Your gross income reduced by any allowable adjustments, deductions, and exemptions.

Tax Return – Your tax return consists of IRS forms that report your income, deductions, and credits for each calendar year.

Tax Treaties – Agreements between the U.S. and certain foreign countries that define the taxation of that country's residents. Generally, an individual must be a tax resident of the treaty country and a nonresident of the U.S. to claim treaty benefits.

Visiting Fellows - Includes individuals present at the NIH to participate in a research program and who are awarded a fellowship stipend to provide for their expenses. Visiting Fellows are not employees of the NIH and do not perform services. Visiting Fellows receive their stipend once per month.

Visiting Scientists – Visiting Scientists are paid wages every two weeks and are considered to be *employees* performing personal services for the NIH; this includes the following categories of individuals:

Research Fellow	Staff Clinician	Investigator
Adjunct Investigator	Senior Investigator	Clinical Fellow
Staff Scientist		

Wages – Compensation for personal services.

HOW TO DETERMINE RESIDENCY STATUS

Federal Tax Residence

The manner in which you are taxed depends upon whether you are, for income tax purposes, considered a resident or nonresident alien. Resident aliens are taxed on their worldwide income in the same manner as U.S. citizens. Nonresident aliens are generally taxed only on U.S. source income.

Residency status for tax purposes is entirely different than residency status for immigration purposes. It is important for you to understand how to determine whether you are a resident or nonresident for tax purposes. Note that your residency status for tax purposes may change from one year to another.

You will be considered a resident alien (for tax purposes) if you meet either the “**green card**” test or the **substantial presence test** for the calendar year:

- (1) **Green Card Test** - A green card gives you the right to reside permanently as an immigrant in the U.S. If you become a permanent resident, you are a resident for tax purposes. Your residency starting date will be the earlier date on which you (1) meet the *substantial presence test*, or (2) become a permanent resident.
- (2) **Substantial Presence Test** –You will meet the substantial presence test if you are present in the US on at least 31 days during the current year, and 183 days during the current and prior two years (according to the substantial presence test calculation). However, you do not count any days that you were considered to be an “exempt individual”.

Exempt Individual: An “exempt” individual includes any individual present in the U.S. with an “F” or “J” visa, who substantially complies with the requirements of the visa. A non-student teacher, trainee, or researcher (“J” visa) is considered to be an “exempt” individual for the first two CALENDAR years of presence in the U.S. A student (“F” visa) is considered to be an “exempt” individual for at least five calendar years.

However:

As a non-student J-visa holder, you will not be an exempt individual if you have been an exempt individual for any two of the previous six calendar years.

As an F-visa holder, you will not be an exempt individual if you have been exempt for any part of more than five calendar years.

NOTE: The term *exempt individual* **does not mean tax-exempt**. It means that the individual is exempt from counting days of presence in the U.S. for purposes of the substantial presence test.

- All exempt individuals must attach **Form 8843** to **Form 1040NR**.

The Substantial Presence Test Calculation: For any year that you are NOT an “exempt” individual, you will count your days of presence in the U.S. according to the following calculation:

TOTAL # OF DAYS DURING THE CURRENT YEAR	+	1/3 # OF DAYS DURING THE PRECEDING YEAR	+	1/6 # OF DAYS DURING THE NEXT PRECEDING YEAR	=	IF TOTAL = 183 DAYS, THEN YOU MEET THE SP TEST
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Do not count any days during any year in which you were an “exempt” individual. A J-visa holder will be

exempt for two out of every seven calendar years. For most “J” visa holders, you will begin to count days on the first day of your third calendar year of presence in the U.S.

EXAMPLE 1: You arrived in the U.S. in November 2004 (as a non-student J-visa holder) 2004 is your first calendar year of presence (even though you have only been present in the U.S. during two months of 2004). 2005 will be your second calendar year of presence. January 1, 2006 will begin your third calendar year and you will now begin counting days of presence for the substantial presence test.

EXAMPLE 2: You were present in the U.S. with a J-visa during 2000. During 2000, you returned to your foreign country. You then return to the U.S. during 2005. 2000 is the first “exempt” calendar year (for not counting days); 2005 is the second “exempt” calendar year (for not counting days). January 1, 2006 is the beginning of the third calendar year, and you will now begin counting days for the substantial presence test.

If You Are Married to a U.S. Citizen or Resident: You can choose to be taxed as a resident alien. You and your spouse must file a *joint* return. You will both be taxed on worldwide income. See IRS Pub 519 for more information regarding choosing resident status.

The following page shows the IRS substantial presence test flowchart from IRS Publication 519, “U.S. Tax Guide for Aliens”.

State Tax Residence

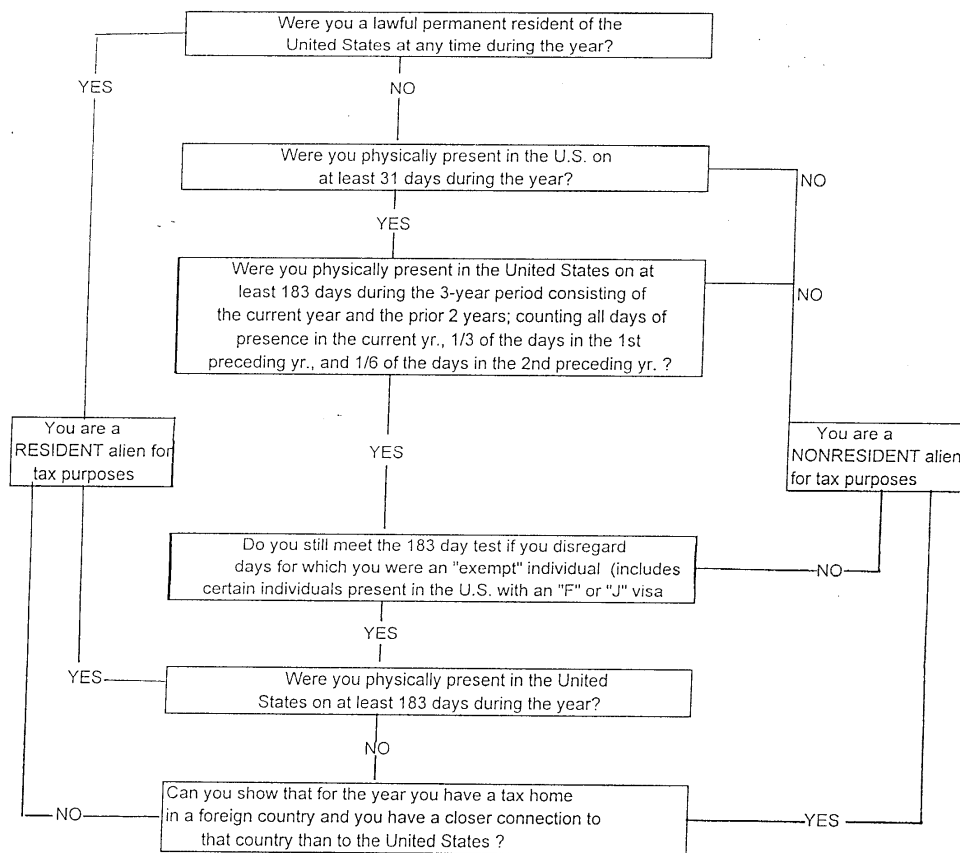
Each state also has rules to determine residency for your state tax purposes. Generally, if you reside in a particular state for a period of six months, you are considered to be a resident for tax purposes:

- **Maryland** – If you establish a place to live in Maryland and you intend to reside, and you do reside for a period of at least six months, you are a resident for tax purposes. Calendar year is not a consideration. There is no initial period of non-residence like the IRS substantial presence test. You may be a part-year resident in your year of arrival (and departure), but if you establish a place to live for more than six months, you are a resident from the first day. If you are present in Maryland for at total time period of less than six months, you are taxed as a nonresident. Nonresidents of Maryland are not required to pay the local county part of the income tax.

Example: A Visiting Fellow arrives at the NIH with a two-year appointment in October of 2004. He/she rents an apartment in Maryland and lives in Maryland for the entire two years. This person is a resident of Maryland for tax purposes from October 2004 through October 2006. They are a part-year resident in 2004, a full-year resident in 2005, and a part-year resident in 2006.

- **District of Columbia** – If you live in DC for at least 183 days, you must file a tax return as a resident. DC does not tax nonresidents.
- **Virginia** – If you reside in Virginia for at least six months, you are taxed as a resident. If you reside in Virginia for less than six months, and you have income from Virginia sources, you are taxed as a nonresident.

NONRESIDENT ALIEN OR RESIDENT ALIEN ?



¹ If this is your first or last year of presence in the U.S., you may be a dual-status taxpayer

² In some circumstances, you may still be considered a nonresident alien under an income tax treaty between the U.S. and your country of residence. Check the provisions of the treaty carefully.

³ If you will meet the substantial presence test in the next year, you may choose to be taxed as a U.S. resident for part of the current year. See IRS Pub 519.

WHICH TAX FORMS SHOULD I FILE?

Federal Tax Forms

Your federal tax return will consist of a number of different forms, which are printed and distributed each year by the Internal Revenue Service. There are hundreds of federal tax forms. Each IRS form has instructions to help you understand how to fill out the form. Each state also publishes their own tax booklet, which includes forms and instructions. The main federal form that you will be required to file depends upon your residency status for tax purposes:

- **Form 1040NR:** Individuals who are **non-resident aliens** according to the substantial presence test must file federal Form 1040NR *U.S. Nonresident Alien Income Tax Return*.
- **Form 1040:** Individuals who are **resident aliens** according to the substantial presence test must file federal Form 1040 *U.S. Individual Tax Return*.

The list below includes additional federal forms that are most common for NIH visiting researchers:

- **Schedule A:** *Itemized Deductions*. There is a separate Schedule A form for residents and for nonresidents. Page 3 of Form 1040NR is the Schedule A for nonresidents. Nonresidents must itemize their deductions. Schedule A shows the different categories of deductions are allowable.
- **Schedule B:** *Interest and Dividend Income*. Resident aliens report interest and dividend income on Schedule B. For a nonresident alien, bank and credit union interest is not subject to federal income tax; it must be reported on pg. 5, Form 1040NR. Nonresidents generally report other taxable interest and dividends on page 4 of Form 1040NR.
- **Schedule C:** *Profit or Loss from Business*. This form is used to report income and expenses from self-employment. If you are paid through a contract agreement, you are considered self-employed.
- **Schedule D:** *Capital Gains and Losses*. This form is generally used by resident aliens to report the sale or exchange of capital assets. Nonresidents report gains and losses on pg. 4 of Form 1040NR.
- **Schedule SE:** *Self-Employment Tax*. Income from self-employment is subject to self-employment tax in addition to the regular federal tax. Nonresident aliens are not liable for self-employment tax. If you are paid as a contractor at the NIH and you file as a **resident**, you must pay self-employment tax.
- **Form 2106:** *Employee Business Expenses*. Use this form to report business expenses and/or travel expenses that are deductible on Schedule A.
- **Form 2441:** *Child Care Credit*. Used to report childcare expenses. The childcare credit cannot be claimed on Form 1040NR. Other rules also apply.
- **Form 8833:** *Tax Treaty Return Position Disclosure*. This form is sometimes required to explain the provisions of a tax treaty benefit. *Nonresident alien* students, trainees, teachers, and researchers are generally not required to attach Form 8833 to Form 1040NR. However, if a treaty benefit is claimed based on the resident article of the treaty or the exception to the savings clause of the treaty, Form 8833 must be attached.
- **Form 8843:** *Statement for Exempt Individuals*. This form is used to explain the basis for excluding days of presence in the U.S. for the substantial presence test. All “exempt” individuals (includes F and J visa holders who have not met substantial presence test) must attach Form 8843 to Form 1040NR.

State Tax Forms

- Maryland Form 502 – Reports the income of Maryland full-year and part-year residents
- Maryland Form 505 – Reports the income of Maryland nonresidents
- DC Form D-40 – Reports the income of DC full-year and part-year residents
- Virginia Form 760 – Reports the income of Virginia residents
- Virginia Form 760PY – Reports the income of Virginia part-year residents

TAX TREATY BENEFITS

The United States has treaty agreements with 60 countries. Different treaty articles apply to different types of income. Treaty benefits for some types of income are explained in IRS Publication 901. You must meet certain qualifications in order to claim the benefits of a particular treaty article:

1) Country of residence - This must be the country where you were a tax resident immediately before coming to the U.S. All treaties include articles that define residence. Residency status is not necessarily determined by citizenship. You may be a citizen of one country and a resident of another country. If you have been present as a student in a country where you are not a citizen or legal resident, you *may or may not* be considered a tax resident of that country. You should know the tax residency rules of that country in order to determine your position.

2) Purpose of visit to the U.S. and character of payment - The purpose of your visit to the U.S., the place where you perform your work, and the source and type of payment that you receive are all factors in determining whether or not you are entitled to treaty benefits.

- The type of visa that an individual holds generally denotes the purpose of the visit to the U.S. An individual with a “J-1” visa will typically be present in the U.S. as a professor, teacher, researcher, student, or trainee.
- When interpreting treaty provisions, it is important to understand that The National Institutes of Health are **not** considered to be a university or an educational institution.
- Treaty articles specify the types of payments that qualify for exemption from tax. You must know if your income is *wages for services performed*, payment of a *grant, allowance, or award*, or payment for *independent personal services* (honorarium or contract agreement).

3) Duration of stay in the U.S. - Most tax treaties impose restrictions on the duration of time you are eligible to stay in the U.S. and claim the benefits of a particular treaty article. Your treaty clock starts ticking on the date you arrive in the U.S. for the purpose of your visit.

Determining Your Treaty Eligibility

Treaty provisions among different countries vary considerably. Each treaty article contains specific qualifications that must be met. A list of treaty benefit articles that apply specifically to NIH Visiting Fellows (grant recipients) is provided on page 28 of this booklet. A list of treaty benefit articles that apply to Visiting Scientists (wage recipients) is provided on page 32. It may be beneficial for you to obtain a copy of the actual text of your tax treaty. Treaty law books are available in most public libraries. **IRS Pub 901** summarizes some of the treaty benefit articles. The IRS makes the final decision on whether the provision in a treaty applies to you.

Special Treaty Provisions for Nonresidents from Canada, Mexico, Japan, Korea, India, Barbados, Jamaica, and Hungary

- **Residents of Mexico and Canada** - can take an exemption for their spouse if the spouse had no gross income for U.S. tax purposes and was not the dependent of another taxpayer. Allowable exemptions for other dependents are subject to the same rules as U.S. citizens. If you have a qualifying dependent and you lived apart from your spouse for the entire year, you may qualify to file as “single”. See Form 1040NR Instructions for more information
- **Residents of Japan and Korea** - can take dependent exemptions if the spouse and dependents have lived in the U.S. with the alien taxpayer at some time during the year. The spouse cannot have any U.S. source income. The deduction for the *spouse* and *dependent* exemptions must be prorated based on the ratio of the alien's:

U.S. source income
Income from worldwide sources

The alien *taxpayer's* personal exemption does not have to be prorated. If you have a qualifying dependent and you lived apart from your spouse for the entire year, you may qualify to file as “single”. See Form 1040NR Instructions for more information.

Note: If a researcher from Japan or Korea qualifies for a treaty exemption, the subtraction of dependent exemptions will not affect the amount of the federal tax. However, the dependent exemptions should still be claimed on the federal return so that they can also be claimed on the Maryland tax return.

- **Students/Trainees from Barbados, Jamaica, and Hungary** - can choose to be taxed as resident aliens according to treaty provisions. Worldwide income must be reported. A married person may file a joint return with their spouse. Dependent exemptions are allowed for each qualifying dependent.
- **Students/Trainees from India** - can take the standard deduction according to a provision in the U.S./India tax treaty. The standard deduction for the corresponding filing status should be entered on the line for itemized deductions on Form 1040NR. On the itemized deduction line, write: *standard deduction allowed per U.S./India tax treaty*. A married person must use the *married filing separately* filing status. An exemption is allowed for a spouse if he/she had no U.S. income and was not the dependent of another taxpayer. Dependent exemptions are **not** allowed for dependent children with F-2 or J-2 visas until they meet the substantial presence test.

Personal Services Treaty Articles

If you are paid according to a contract agreement, you may be entitled to a treaty exemption under the provisions for “*Personal Services Income*” for income from *independent personal services*. Most benefits extended under these provisions are limited as to length of time present in the U.S. and/or the maximum amount of income that can be received. You must qualify as a nonresident alien according to the Substantial Presence Test. The exception to the savings clause does not apply.

Treaty Benefits for State Income Taxes

The State of Maryland does not recognize federal tax treaties - Therefore, even though your income may be excluded from taxation by the federal government, you still must file and pay Maryland taxes. The state of Virginia and the District of Columbia honor federal treaty agreements.

FORM W-7 “APPLICATION FOR INDIVIDUAL TAX IDENTIFICATION NUMBER

Each individual claimed as an exemption on Form 1040 or Form 1040NR must have a social security number or an individual tax identification number (ITIN). A spouse with work permission will be entitled to apply for a social security number. A child born in the US will be issued a social security number at birth.

If you qualify to claim the exemption of a family member who does not have an identifying number, you must submit Form W-7 with Form 1040 or Form 1040NR to apply for the number. Form W-7 cannot be submitted in advance. You must include proof of identity such as a visa or passport. You can have copies of the official picture identification notarized, or you can have the originals certified by an acceptance agent at an IRS office.

- If you are filing as a nonresident on Form 1040NR, you cannot claim additional exemptions unless you are from Canada, Mexico, India, Japan, or Korea (other rules may also apply).
- The exemption amount for tax year 2004 is \$3,100 per person. This amount is generally not prorated, although a special rule applies to Japan and Korea.
- If you are filing as a resident alien, and you have a qualified spouse and/or dependents, you must have a number for each individual claimed. Each dependent must meet all five dependency tests explained on page 16.

FILING AS A NONRESIDENT ALIEN

General Information for Nonresident Aliens

A nonresident alien is an individual who does not meet (1) the green card test or, (2) the IRS Substantial Presence Test. Nonresidents must file **Form 1040NR**. The following rules apply to all nonresident tax returns:

- **Filing Status** - A nonresident is limited to using the *single* or *married filing separately* filing status and applicable tax rates. If you are married, you may not file a joint return or a return as a single person; a married separate return **must** be filed. If your spouse is not with you in the U.S., you must still use the married separate filing status (you cannot file as single).
- **Personal Exemptions** - Generally, only **one** personal exemption is allowed. The federal personal exemption amount for 2004 is \$3,100. The full exemption amount is allowed even if you have only been present in the U.S. for part of the tax year. If you are a resident of Canada, Japan, Korea, Mexico, or India, you may be entitled to additional exemptions. This is explained in the treaty section of this handbook.
- **Nonresidents are generally taxed only on U.S. Source Income** – Nonresidents are taxed on income *effectively connected with a U.S. trade or business* at the same graduated rates as U.S. citizens and residents. However, any U.S. source investment income (*income not effectively connected with a U.S. trade or business*) is taxed at a flat 30% rate unless reduced by a different treaty rate. Some types of U.S. income such as bank deposit interest are tax-exempt. Capital gains are not taxable to nonresident aliens who are present in the U.S. for less than 183 days during the calendar year.

- **Tax treaty provisions may exempt some income from tax** – Tax treaty benefits generally apply to individuals who are nonresidents of the U.S. and “tax” residents of the treaty country. The rules for determining U.S. residency for tax purposes, however, do not override treaty definitions of residency. For example, if you are a U.S. tax resident according to the substantial presence test and you are a tax resident of your treaty country (under the treaty definition of residency), you may qualify to claim treaty benefits as a nonresident alien. You must remain taxable in your foreign country to remain a tax resident under the resident article. This is called “dual-resident” taxpayer. A dual-resident taxpayer will file as a nonresident on Form 1040NR and attach Form 8833.
- **Adjustments** – Adjustments are items that reduce your gross income:
 - (1) Educator expenses – A deduction of up to \$250 for teachers who purchase supplies for their classroom.
 - (2) IRA deduction - An IRA deduction is an individual contribution to a retirement account. It does not include amounts contributed through an employer sponsored retirement plan.
 - (3) Student loan interest deduction - The student loan interest deduction is allowed for nonresidents if their filing status is “Single”. Other restrictions also apply.
 - (4) Moving expenses - Moving expenses are available for nonresident aliens who are employees of NIH.
 - (5) Health insurance payments for an individual who is paid through a contract agreement are 100% deductible. You must be considered self-employed. Grant recipients and NIH employees receiving wages do not qualify as self-employed.
 - (6) Self-employed SEP, SIMPLE, and qualified plans-These are retirement plans that are available to individuals who are self-employed.
 - (7) Penalty on early withdrawal of savings
 - (8) The tuition part of a scholarship is not taxable. If you have been awarded a scholarship and it is reported to you as income, you can deduct the part that applies to tuition, books, and fees. NIH fellowship grants are not considered to be scholarships.
- **Deductions** - The standard deduction is not allowed. Nonresidents **must** itemize deductions on **Schedule A**. Itemized deductions are limited to:
 - (1) State and local income taxes (withheld or paid *during the tax year*)
 - (2) Contributions to qualified **U.S.** charitable organizations
 - (3) Casualty and theft losses from U.S.-based property,
 - (4) Miscellaneous “business” expenses - includes travel expenses for business trips. If your stay in the U.S. is for one year or less and you meet certain IRS rules, your appointment at NIH may qualify as a business trip.
 - (5) Other miscellaneous deductions.

Compensation From a Foreign Employer

Nonresident aliens are generally taxed only on income from U.S. sources. If you have a “J” visa and *all* of your income is from a foreign source, you will not owe any tax and you are not required to file Form 1040NR. However, **Form 8843**, which verifies exempt individual status, must be filed by April 15th of each tax year. Attach a copy of your DS-2019 form to Form 8843.

As an exchange visitor, the exemption of your foreign income should fall into one of the following categories:

- 1) Payments made by a foreign employer to a person in the U.S. under “F”, “J”, or “Q” visas are exempt from federal taxation. These individuals enter the United States under section 101(a)(15)(J) of the

Immigration and Nationality Act. Nonresident aliens temporarily present in the U.S. under this section of the Act include bona-fide students, trainees, scholars, professors, research assistants, specialists or leaders in a field of specialized knowledge or skill.

2) A foreign source scholarship, fellowship, or grant is not subject to U.S. tax. The source of the grant is the residence of the payer regardless of who actually disburses the funds. Payments made by an entity designated as a public international organization under the International Organizations Immunities Act are from foreign sources.

3) Remittances or allowances for studying or training from a foreign payer may be exempt from tax by a tax treaty agreement. These benefits are generally included in the Student/Trainee articles of the treaties. Once you meet the substantial presence test, however, you become liable for tax on your worldwide income. A foreign source research grant may continue to qualify for exemption from tax under the benefit article and the exception to the savings clause. Consult your treaty carefully to determine if you meet all qualifications.

- **If your foreign income falls under category (1) or (2) above, file Form 8843, and attach a copy of your DS 2019.**
- **If NIH pays you *and* you receive income from a foreign employer or a foreign source grant or allowance, you must file Form 1040NR, Form 8843, and attach a copy of your DS-2019.**

FILING AS A RESIDENT ALIEN

General Information for Resident Aliens

If you meet the green card test or the substantial presence test, you must file your tax return as a resident. Residents fill out Form 1040. As a resident you are taxed on your worldwide income. The following rules apply to resident taxpayers filing Form 1040:

- **Filing Status** - If you are married, you may file a *joint* return with your spouse. You are not restricted to using the *married filing separately* filing status.
- **Exemptions** - You may claim additional personal exemptions for dependents according to the same rules as U.S. citizens. If your spouse is not in the U.S., you must file as *married filing separately*. However, you may claim an exemption for your spouse if he or she had no income for U.S. tax purposes and is not the dependent of another taxpayer. The personal and dependent exemption amount for 2004 is \$3,100. You must have an identifying number for each dependent you claim on your tax return. If your spouse or dependent does not qualify for a social security number, they can apply for tax identification number by filing Form W-7 with the IRS. Your spouse is not considered to be your dependent. If you file a joint return with your spouse, you are each entitled to your own personal exemption. Other individuals must meet **all of the following 5 tests** in order for you to claim them as a dependent:
 - (1) **Member of Household or Relationship Test**- The person must live with you for the entire year, or be related to you.
 - (2) **Citizen or Resident Test** - The person must be a U.S. citizen or resident (apply the substantial presence test) or a resident of Canada or Mexico.
 - (3) **Gross Income Test** - The person cannot earn more than \$3100 for the year. This limit does not apply to full-time students under age 24.
 - (4) **Joint Return Test** - The person you are claiming as a dependent cannot be filing a joint return with a spouse.
 - (5) **Support Test** - you must have provided more than 1/2 of that person's support.

■ **Adjustments**

- (1) Educator expenses – A deduction of up to \$250 for teachers who purchase supplies for their classroom.
- (2) IRA deduction - An IRA deduction is an individual contribution to a retirement account. It does not include amounts contributed through an employer sponsored retirement plan.
- (3) Student loan interest deduction - The student loan interest deduction is allowed for nonresidents if their filing status is “Single”. Other restrictions also apply.
- (4) Tuition and fees deduction – A deduction for college expenses; cannot be taken simultaneously with the education credits-other restrictions apply.
- (5) Moving expenses - Moving expenses are available for nonresident aliens who are employees of NIH.
- (6) One-half of self-employment tax – If you pay self-employment taxes, ½ are deductible as an adjustment.
- (7) Health insurance payments for an individual who is paid through a contract agreement are 100% deductible. You must be considered self-employed. Grant recipients and NIH employees receiving wages do not qualify as self-employed.
- (8) Self-employed SEP, SIMPLE, and qualified plans-These are retirement plans that are available to individuals who are self-employed.
- (9) Penalty on early withdrawal of savings
- (10) Alimony paid – Recipient must have a US social security number.

- **Deductions** - You may claim a **standard deduction** OR you can itemize deductions. You can never claim both the standard deduction and itemized deductions. The amount of your standard deduction depends upon your filing status. The standard deduction amounts for 2004 are:

Single	\$4,850	Married filing separately	\$4,850
Married Filing Jointly	\$9,700	Head of Household	\$7,150

- OR -

You may claim the following **itemized deductions**:

- (1) Medical and dental expenses (within certain limits),
- (2) State income taxes paid or withheld during the tax year and certain other taxes (including real estate taxes),
- (3) Certain home mortgage interest and investment interest expense,
- (4) Contributions to qualified U.S. charitable organizations,
- (5) * Miscellaneous business expenses, and
- (6) Other miscellaneous expenses

* You may deduct travel expenses for business trips of one year or less if you meet certain IRS rules. Miscellaneous deductions are subject to a subtraction of 2% of your adjusted gross income.

- **Credits** - As a resident alien you may be entitled to tax credits, including:

- (1) Foreign Tax Credits - You may claim a credit, subject to certain limits, for income tax you paid or accrued to a foreign country on foreign source income. You may not claim a credit for taxes paid on excluded income. The foreign tax credit is claimed on Form 1116.
- (2) Child Care Credit - If you file as a resident alien and you and your spouse both work, and you pay someone to care for your dependent(s) under age 13, you may be able to take a child care credit of up to 30% (depending on your income) of the amount you paid. You must both have income that qualifies as *earned income*. NIH grants do not qualify as earned income. You must file as *Married Filing Jointly* or as *Head of Household* to take the child care credit. The childcare credit is claimed on Form 2441.

- (3) Education Tax Credits - there are two different credits available for post secondary education expenses incurred on behalf of a taxpayer, spouse, or dependent. The two credits may not be claimed in the same year. Other restrictions also apply. See IRS Pub 970.
- (4) Child Tax Credit - the credit is up to \$1,000 for each qualifying child under age 17. The credit is phased out at income levels in excess of \$ 110,000 for MFJ.

Claiming a Treaty Benefit as a Resident Alien

Certain treaty benefits extend to individuals who meet the substantial presence test under the exception to the savings clause of the treaty. If the treaty includes an exception to the savings clause, you are not required to remain a “tax” resident of the treaty country under the resident article in order to qualify for certain specified benefit articles. An individual claiming a treaty benefit under the exception to the savings clause will file as a resident on Form 1040 and attach Form 8833.

Explanation of the “Savings Clause” - The *Savings Clause* of a treaty reserves the right of a country to tax the residents of that country as if the treaty were not in effect. This means that once you meet the substantial presence test, you may not be allowed to claim treaty benefits because you are a tax resident of the U.S. according to U.S. tax law.

Exception to the “Savings Clause” - Many treaties have articles that provide an exception to the *Savings Clause* for certain benefits. Most of the treaties that extend benefits to students, trainees, teachers, and researchers include an exception to the savings clause. The exception to the savings clause will state that an individual may continue to claim the benefits of a particular article after becoming a resident of the U.S. for tax purposes. The exception to the savings clause does not extend to individuals who have permanent residency.

Dual-Status Resident

You have a dual-status tax year when you are both a resident alien and a nonresident alien in the same tax year. If you come to the U.S. with an “H” visa, you may have dual-status in your year of arrival. A “J” visa holder will generally not have dual-status in the year of arrival, but may have dual-status in the year of departure. Dual-status refers only to your resident status in the United States for tax purposes. Do not confuse *dual-status* taxpayer with *dual-resident* taxpayer. In determining your U.S. income tax liability for a dual-status tax year, different rules apply for the part of the year you are a resident for tax purposes and for the part of the year you are a nonresident for tax purposes. As a dual-status alien you are taxed on worldwide income for the part of the year you are a resident alien, and on income only from U.S. sources for the part of the year you are a nonresident alien. Fill out Form 1040 for the resident part of the year, and Form 1040NR for the nonresident part of the year. See IRS Publication 519 for more information.

Restrictions for Dual-Status Taxpayers

The following restrictions apply if you are filing a tax return for a dual-status year:

- **Filing Status** - You cannot use the *head of household* filing status, and you cannot file a *joint* return with your spouse. You must file and use the tax rate schedules as *single* or *married filing separately*.
- **Standard Deduction** - You cannot use the standard deduction. As a dual-status taxpayer, you must itemize any allowable deductions. You will have different allowable deductions for each part of the year. Report deductions during period of *non-residence* on Schedule A, Form 1040NR. Report deductions during period of *residency* on Schedule A, Form 1040.
- **Personal Exemptions** - As a dual-status taxpayer, you will be able to claim your own personal exemption. Subject to the dependency rules, you can claim exemptions for your spouse and dependents

when you figure taxable income for the part of the year you are a *resident alien*. The amount you can claim for these exemptions is limited to your taxable income (figured before subtracting exemptions) for the part of the year you are a resident alien. Do not prorate your exemptions.

Last Year of Residency

If you have been filing as a resident alien, your residency termination date is generally the last day of the tax year. However, you are not treated as a U.S. resident for the part of a calendar year *after the last day you are present* in the United States if you:

- Had a closer connection to a foreign country than to the United States for the rest of that calendar year, and
- Your tax home was in that foreign country during the rest of that calendar year.

To determine the last day of presence in the United States, you do not have to count up to 10 days of actual presence in the United States if you establish that you had a closer connection to a foreign country than to the United States on those days.

If you terminate your U.S. residency prior to the last day of the year, you must file a residency termination statement with your tax return stating that you had a closer connection to your foreign country for the remainder of the calendar year. See IRS Publication 519 for information regarding the residency termination statement. A resident alien who leaves the United States temporarily and does not abandon his or her residence keeps resident alien status even while abroad.

MISCELLANEOUS EXPENSES (Itemized Deduction)

If you are filing as a nonresident alien, you must itemize your deductions. Resident aliens can choose between itemizing deductions or claiming the standard deduction amount. Itemized deductions are claimed on Schedule A. This section provides a more detailed explanation of what deductions qualify as “Miscellaneous Deductions”

Allowable miscellaneous deductions must be related to your income that is effectively connected with a U.S. trade or business and includes expenses such as:

- Safety equipment and small tools needed for your assignment
- Dues to professional organizations
- Subscriptions to professional journals
- Tax preparation fees and investment account fees
- Certain qualifying educational expenses
- Un-reimbursed business travel expenses

Un-reimbursed Business Travel Expenses: You may be able to deduct your ordinary and necessary expenses for meals, lodging and transportation that are attributable to business travel. Business travel includes travel to attend meetings, conferences, conventions, and seminars that are related to your job. For example: If you travel from NIH to New York City to attend a job-related meeting, your **un-reimbursed** travel expenses are deductible. If you combine business and pleasure when you travel or if you travel outside of the U.S. for business, you may be allowed to deduct only a portion of your travel expenses. IRS Publication 463 explains the rules for prorating overseas travel expenses.

Your appointment at NIH may qualify as business travel. You may be able to deduct your ordinary and necessary expenses for meals, lodging and transportation attributable to your entire appointment at NIH if you can show that you are present in the United States on an activity that required you to be absent **temporarily** from your **regular place of work**.

- **When Is A Job Temporary?** A job is considered temporary if you travel away from your tax home for a reasonably short period of time. A period of **one year or less** is considered by the IRS to be a short time for this purpose.

If you work away from home for more than one year, then your stay is considered permanent or indefinite in length and does not qualify for the “temporary job away from home” deduction. If your appointment is for two years, you cannot deduct these expenses for the first year! The deductions are available for appointments of one year or less only.

- **Tax Home:** To deduct travel expenses you must determine the location of your tax home. You establish a tax home through regular employment in a certain area.

If you have not had regular employment in a certain area, then your tax home *may be* the place where you regularly live. There are three factors that determine if your tax home is where you regularly live. If you do not have a regular place of business or you do not meet the factors that determine that your tax home is where you live, then you are considered a transient and your tax home is wherever you work. As a transient, you are never away from home, so you cannot claim travel expense deductions.

Three factors that determine if your tax home is where you live

- 1) You perform part of your business in the area of your main home and you use that home for lodging while doing business there.
- 2) You have living expenses at your main home and at your temporary location.
- 3) You have not abandoned your main home; you have family members living there or you use that home often for lodging.

If you satisfy all three factors, then you have a tax home where you regularly live. If you satisfy only two factors, you *may* have a tax home depending on all the facts and circumstances. If you satisfy only one factor, your tax home is wherever you work and you cannot deduct travel expenses.

- If you come to NIH *initially* for a one-year appointment and then you receive a second appointment, that extends your stay beyond one year, your situation changes from *temporary* to *indefinite*. If you have met all the other requirements stated above, you may deduct your travel expenses up until the day you first take steps to extend your appointment beyond one year.
- If you come to NIH initially for a 15-month appointment and then your stay is shortened to 9 months, you *do not* qualify to deduct your travel expenses because it was expected that you would stay for more than one year.

What Expenses Can You Deduct? If you qualify for business travel expenses, you may deduct your **own** un-reimbursed expenses for:

- (1) **Lodging** - Lodging costs include rent, utilities, heat, electricity, renters insurance, cleaning, and waste removal. They do not include personal telephone expenses, or clothing needed because our climate is different from that in your own country. Allowable lodging costs are equal to the cost of lodging for yourself if you were living in the U.S. without your family i.e. (the rent for one-bedroom apartment and approximately 75% of utilities).

- (2) **Transportation** – Includes your un-reimbursed airfare to and from the U.S., and your local transportation. Local transportation includes the cost of bus, metro, and taxi. Keep a written record of these expenses. If you buy a car, you can deduct 37.5 cents per mile for 2004 for all business mileage incurred. You must keep a written record of your mileage. The mileage rate for 2005 has increased to 40.5 cents per mile.
- (3) **Meals** - You can deduct your actual expenses or you can use the government Per Diem rates. The Per Diem rates for 2004 are listed below for specific areas. Per Diem rates for travel elsewhere within the U.S. are available at www.policyworks.gov/perdiem. Per Diem rates for travel outside of the continental U.S. are available at www.state.gov/www/perdiems. The total amount of your meal deduction is reduced by 50 % when you fill out **Form 2106** and report the expenses.

<u>Location</u>	<u>October 1, 2004 – Sept. 30, 2005</u>
Montgomery County, MD	\$ 51
Washington, DC	51
Frederick, MD	35
Baltimore, MD	47
Durham, NC	47
Hamilton, MT	35
Phoenix, AZ	47

- (4) **Long distance business phone calls** - Long distance *business* call charges only. Do not include any installation or hook-up fees for phone service.

You cannot deduct expenses for other members of your family. Miscellaneous deductions are subject to a subtraction of 2% of your adjusted gross income.

Note: If you live in Maryland and:

- You are entitled to the benefits of a tax treaty, and
- You qualify to deduct travel expenses; you should fill out Form 2106 with your federal tax return so that you can also claim the deductions on your state tax return.

Education Expenses

Expenses that you incur for education that is required by your employer or that will maintain or improve your present job skills qualifies as a miscellaneous deduction. Education that qualifies you to practice a new profession does not qualify. You can include expenses for tuition, books, and fees. In some cases you can also include transportation expenses if you travel from work directly to school. See IRS Pub 508 for more information.

Alternative Minimum Tax

The alternative minimum tax rules are a complicated part of the U.S. tax system. Claiming miscellaneous itemized deductions is just one situation that can trigger the “AMT”. If you are subject to the AMT, you must include Form 6251 with your Form 1040 or Form 1040NR. If you claim business travel expenses and your income is greater than the amount stated below, you should fill out Form 6251 to determine if you are subject to alternative minimum tax:

<u>Filing Status</u>	<u>Income</u>
Single	\$40,250
Married Filing Jointly	58,000
Married Filing Separately	29,000

KEEPING RECORDS

Adequate records must be kept for all expenses, but no particular form is required for keeping them. You should keep sales slips, invoices, receipts, and canceled checks to verify the deductions and credits shown on your tax return. Keep copies of all income reporting forms and any other documents that prove the amounts shown on your return as income. Your records must be kept available in a manner that will allow the Internal Revenue Service to determine your correct tax.

Your checkbook: Your checkbook can be a basic source for keeping a record of your deductible expenses. If your checkbook has enough space, record sufficient information when you write a check. Canceled checks alone are not always adequate evidence. You should keep receipts, sales slips and any other documents that prove an expense. If you make payments with cash, get a complete dated, and signed receipt for any cash payments that may be deductible.

Adequate Records: You should keep the records and proof you need for your expense items in an appointment book, diary, logbook, statement of expense, trip sheet, or similar record supported by adequate documentary evidence. If you travel by public transportation, an entry in a daily logbook of the amount of the expense is sufficient evidence.

Timely Record keeping: You do not have to write down the elements of every expense at the time of the expense. However, a record made at the time of the expense has more value than a statement prepared later. A log maintained on a weekly basis, which accounts for use during the week, is considered a record made at or near the time of the expense. You do not have to record information that duplicates information shown on a receipt as long as your records and receipts complement each other in an orderly manner.

Record keeping for automobile expenses: In order to claim a deduction for a car that you use in your business or work, you must be able to prove certain items. You must be able to prove these items by adequate records or sufficient evidence that will support an item as an expense. Estimates or approximations do not qualify as proof of an expense. You must be able to prove:

- The amount of each separate expense for a car, such as the cost of buying a car or lease payments.
- The cost of maintenance and repairs, or other expenses.
- The date of each expense or use.
- The business or investment reason for the expense or use of the car.
- **The mileage for each business use of the car and the total miles for the tax year.**

Sample Mileage Record			
<u>Date</u>	<u>Destination</u>	<u># Miles</u>	<u>Odometer Reading</u>
Beginning			54,252
04/15/2004	NIH	10	54,262
04/16/2004	NIH	10	54,272
04/16/2004	Safeway	5	54,277
04/16/2004	BBT Bank	7	54,284
04/17/2004	NIH	10	54,294

It is important to record the ending mileage on December 31 of each year.

Business Purpose: A written statement of the business purpose of an expense is generally required. A daily appointment book can be a source of a record that can help prove the business purpose. However, the degree of proof varies according to the circumstances in each case. If the business purpose of an expense is clear from the surrounding circumstances, a written explanation may not be required.

Incomplete Records: If you do not have adequate records to prove an element of an expense, then you must prove the expense by:

- Your own statement, whether written or oral, containing specific information in detail.
- Other supporting evidence sufficient to establish the expense.
- In some cases, circumstantial evidence may support the amount of business and investment use. For example, where your work requires travel to a distant library or laboratory, entries in a ledger or notebook provides circumstantial evidence of the fact that you use your car for business purposes.

Sampling: You can maintain an adequate record for parts of a tax year and use that record for the entire tax year if you can demonstrate by other evidence that the record period is representative of the use throughout the tax year.

Destroyed Records: You can substantiate a deduction by reconstructing your records or expenses if you cannot produce a receipt for reasons beyond your control, such as fire, flood or other casualty.

How Long To Keep Records: You must keep proof to support your claim to a deduction as long as your income tax return can be examined. Generally it will be necessary for you to keep your records for at least three years from the date you file the income tax return on which the deduction is claimed. A return filed early is considered filed on the due date.

SOCIAL SECURITY AND MEDICARE TAXES

Social security and Medicare taxes (FICA) are taxes that are assessed in addition to federal income taxes on “earned income”. This tax is a contribution to the US social security and Medicare system that provides retirement and medical benefits for individuals over a certain age, and disability benefits for the totally disabled. If you are subject to social security and Medicare taxes, your contributions do not count as a credit or payment to be applied to your federal income tax.

The tax is collected differently for individuals who are employees and for individuals who are considered self-employed:

Employees - Generally, the employer pays one-half of the tax and the employee pays one-half through withholding.

Self-employed – Self-employed individuals pay their own self-employment taxes with their year-end tax form. If you work under a contract agreement at the NIH, you are considered self-employed.

The following individuals are exempt from social security and Medicare taxes:

- Services performed by a *nonresident alien* with an F-1, J-1, M-1, or Q-1 visa are generally exempt from social security taxes. This special rule applies only to individuals who have **not met** the IRS substantial presence test.
- Fellowship grants paid by the NIH are not considered earned income and are, therefore not subject to social security and Medicare taxes. This rule applies to both nonresident and resident aliens.
- *Nonresident alien* individuals who are considered self-employed are not subject to social security and Medicare taxes.

The following individuals are subject to social security and Medicare taxes:

- Services performed by a *resident alien* with an F-1, J-1, M-1, or Q-1 visa are subject to social security and Medicare taxes. This means that if you come to the US with a J-1 visa and you are working as an employee of the NIH, you will become subject to the social security and Medicare taxes on January 1 of the year that you meet the IRS substantial presence test.
- A spouse or dependent with a J-2 visa will be subject to social security and Medicare taxes on employment earnings reported on Form W-2. This applies to both nonresident and resident alien J-2 visa holders.
- If you are working under a contract agreement with NIH **and** you are filing as a **resident**, your *net contract income* (contract income reduced by contract expenses) is subject to self-employment tax. Self-employment income is reported on Schedule C. Self-employment tax is reported on Schedule SE.

INFORMATION SPECIFIC TO VISITING FELLOWS AND OTHER GRANT RECIPIENTS

How Income is Reported to Visiting Fellows

Employers and other payers of income are required to report the income that you have earned during the calendar year. One copy is provided to you; another copy is provided to the Internal Revenue Service. This is called the matching system. When you file your final tax report, the IRS will match the amount of income you have reported on your tax documents with the amount of income that the payer of the income has reported. Visiting Fellows will receive **Form 1042S** from the NIH by March 15 reporting the amount of the fellowship grant received during the previous calendar year. The 1042S form should report all income paid to you from January 1 through December 1. Other forms that may be issued to you reporting income that you have earned include:

- Form 1099 Miscellaneous – Reports miscellaneous income paid to you during the calendar year. Some grantors report stipends paid on Form 1099 Miscellaneous.
- Form 1099 INT – Reports interest income paid to you during the calendar year.
- Form 1099 DIV – Reports dividend income paid to you during the calendar year.

A copy of Form 1042S is shown on the following page.

Form 1042-S		Foreign Person's U.S. Source Income Subject to Withholding				2004		OMB No. 1545-0096	
Department of the Treasury Internal Revenue Service		<input type="checkbox"/> VOID <input type="checkbox"/> CORRECTED <input type="checkbox"/> PRO-RATA BASIS REPORTING		Copy C for Recipient <small>Attach to any Federal tax return you file</small>					
1 Income code	2 Gross income	3 Withholding allowances	4 Net income	5 Tax rate	6 Exemption code	7 U.S. Federal tax withheld	8 Amount repaid to recipient		
9 Withholding agent's EIN ▶ <div style="display: flex; justify-content: space-between; margin-top: 5px;"> <input type="checkbox"/> EIN <input type="checkbox"/> QI-EIN </div>				14 Recipient's U.S. TIN, if any ▶ <div style="display: flex; justify-content: space-between; margin-top: 5px;"> <input type="checkbox"/> SSN or ITIN <input type="checkbox"/> EIN <input type="checkbox"/> QI-EIN </div>					
10 WITHHOLDING AGENT'S name and address (including ZIP code)				15 Recipient's country of residence for tax purposes			16 Country code		
				17 NONQUALIFIED INTERMEDIARY'S (NQI's)/ FLOW-THROUGH ENTITY'S name			18 Country code		
				19 NQI's/Flow-through entity's address					
11 Recipient's account number (optional)			12 Recipient code		20 NQI's/Flow-through entity's TIN, if any ▶ 21 PAYER'S name and TIN (if different from withholding agent's)				
13 RECIPIENT'S name (first name, initial, and last name), street address, city or town, province or state, and country (including postal code)									
22 State income tax withheld			23 Payer's state tax no.		24 Name of state				

Form **1042-S** (2004)

Official form is smaller than full page. Please cut to size along solid lines before filing.

How Taxes Are Paid

Federal and state taxes must be paid throughout the year as you earn your income. The NIH is required to withhold federal tax from each fellowship payment and deposit it with the US Treasury. The federal tax withheld is not your actual tax liability. You will calculate your actual tax on your final tax Form 1040NR or Form 1040 at the end of the calendar year. You report the tax withheld on your final tax form as a payment. The withholding rate for fellowship grants is 14%. The amount of tax withheld is also reported to you at the end of the year on Form 1042S.

If you are entitled to a tax treaty benefit, you may be excused from federal tax withholding. You must submit Form W-8BEN to NIH to claim exemption from federal tax withholding. Even if you are exempt from federal tax and withholding because of a treaty benefit, you must still file your final tax form at the end of the calendar year.

If you have paid more taxes through withholding than your actual tax liability, you will receive a refund of the over withheld taxes after your final tax return is processed.

The National Institutes of Health does not withhold state taxes from fellowship grant recipients. Because there is no withholding, you must determine if you are required to make estimated tax payments during the calendar year (in advance) for your state tax liability.

Estimated Tax Payments

The National Institutes of Health withholds federal income taxes from all Visiting Fellows who are liable for federal tax. If you are paid by another source, your payer may not withhold federal tax. You may be required to make estimated federal tax payments. The federal forms for calculating and paying estimated taxes is Form **1040ES(NR)** for nonresidents, or Form **1040ES** for residents. These forms include coupons for each quarterly payment, a worksheet to help you estimate your tax, and instructions on when and where to send payments.

The National Institutes of Health withholds state taxes from the payments of all visiting scientists receiving wages. However, the NIH does not withhold any state income taxes from the pay of fellowship grant recipients. If you are receiving a fellowship grant, you will probably be required to estimate and pay taxes during the year as you receive your fellowship grant. Estimated taxes are payable quarterly (four times per year) and due on the following dates:

April 15	pay 1/4 of estimated taxes for current year
June 15	pay 1/4 of estimated taxes for current year
September 15	pay 1/4 of estimated taxes for current year
January 15	final payment is due

Form **502D** will help you compute your Maryland estimated tax for 2004 or 2005. It includes one coupon for making the first payment. The State of Maryland will then mail you coupons for the remaining payments if you request them by checking the box on the right hand side of the coupon.

You should take into consideration all anticipated income and deductions for the tax year when computing estimated tax. Making estimated payments does not fully satisfy your tax obligations. You must still fill out and file the final income tax report by April 15th.

If you fail to make estimated payments, you could be subject to interest and/or penalties in addition to the tax you owe. You could also find yourself owing a large tax bill when you file your tax return. Any estimated payments that have been made during the year are reported in the "payments" section of the tax form.

Note: If you are paid by Courtesy Associates, you will not have any **federal or state** taxes withheld.

How to Fill Out Form 502D

Example: Visiting Fellow from Germany arrived in the U.S. in February for a two-year appointment and will be paid a NIH fellowship grant of \$3,000 per month

1) Start with your gross income for the tax year (the total amount that you will be paid during the calendar year up to December 31). Use the amount you will be paid before any subtractions for federal taxes, health insurance, etc.

\$3,000 per month x 10 months.....\$30,000

2) Subtract standard deduction..... (2,000)

28,000

3) Subtract (1) personal exemption..... (2,400)

Maryland Taxable Income 25,600

Calculate Maryland State Tax on \$27,600:	\$25,600	
(See Tax Rate Schedule on page 35)	<u>-3,000</u>	
	22,600	
	<u>x .0475</u>	
	\$ 1,074	
	<u>+ 90</u>	

Total Maryland State Tax \$ 1,164

Calculate Montgomery County Tax on \$25,600:	\$25,600	
	<u>x .0320</u>	

Total Montgomery County Tax 819

Total Maryland and Local Tax \$ 1,983

- **\$1,983/4 payments = \$496 each quarterly payment**

Mail your check to the Comptroller of Maryland to the address shown on Form 502D. Include only the coupon with your check or money order. **It is important to write your social security number on your check and the form number.** It is also possible to pay estimated payments on the state of Maryland website, however, there is a fee for this service. If you reside in another state, you will need to download the worksheet and form for calculating your estimated payments:

- Download **Form D-40ES** from the DC website if you live in the District of Columbia
- Download **Form 760ES** from the Virginia website if you live in Virginia

Tax Treaty Benefits for Visiting Fellows

Treaty benefits for Visiting Fellows and grant recipients are generally included in the articles that apply to “Students and Trainees”. Most treaties extend the student/trainee benefits to include researchers who are performing public research at a governmental, scientific organization and receiving a “grant, allowance, or award” as the type of payment. The treaty articles that fall under the “Professor/teacher” provisions do not apply to NIH fellowship grant recipients.

Treaty Articles for Visiting Fellows and Other Grant Recipients

<u>Treaty Country</u>	<u>Article</u>	<u>Eligibility From Date of Arrival</u>	<u>Max. Amount Of Tax Exemption</u>
Belgium	21 (1)	5 full years	No Limit
China	20(b)	Reasonable Necessary Period	No Limit
C.I.S. (former USSR)	VI (1)	5 full years	Living Expenses Up to \$10,000
Cyprus	21 (1)	5 tax years	No Limit
Czech Republic	21 (1)	5 full years	No Limit
Egypt	23 (1)	5 tax years	No Limit
Estonia	20 (1)	5 full years	No Limit
France	21 (1)	5 tax years	No Limit
Germany	20 (3)	No Limit	No Limit
Iceland	22 (1)	5 full years	No Limit
Indonesia	19 (1)	5 full years	No Limit
Israel	24 (1)	5 tax years	No Limit
Kazakhstan	19	5 full years	No Limit
Korea	21 (1)	5 full years	No Limit
Latvia	20 (1)	5 full years	No Limit
Lithuania	20 (1)	5 full years	No Limit
Morocco	18	5 full years	No Limit
Netherlands	22 (2)	3 full years	No Limit
Norway	16 (1)	5 tax years	No Limit
Philippines	22 (1)	5 full years	No Limit
Poland	18 (1)	5 full years	No Limit
Portugal	23 (1)	5 tax years	No Limit
Romania	20 (1)	5 full years	No Limit
Russia	18	5 full years	No Limit
Slovak Republic	21 (1)	5 full years	No Limit
Slovenia	20	5 tax years	No Limit
Spain	22 (1)	5 full years	No Limit
Thailand	22 (1)	5 full years	No Limit
Trinidad & Tobago	19 (1)	5 tax years	No Limit
Tunisia	20	5 full years	No Limit
Ukraine	20	5 full years	No Limit
Venezuela	21 (1)	5 full years	No Limit

Do not rely on this list as an interpretation of your individual eligibility to claim an exclusion from tax. In some situations it may be necessary to consult the treaty itself to determine if all qualifications are met.

New Tax Treaty with Japan - The United States has exchanged instruments of ratification for a new income tax treaty with Japan. As a result of this new agreement, there is a change in Article 20 of the former treaty, which provided benefits for NIH grant recipients. In the new treaty, Article 19 applies to grant recipients and Article 20 applies to wage recipients. The effective date for the new provisions of Articles 19 and 20 is March 31, 2004.

Article 19 - A student or business apprentice who is a resident of Japan immediately before visiting the U.S. and is in the U.S. for the purpose of education or training is exempt from U.S. income tax on amounts *received from abroad* for the individual's maintenance, education, or training. This benefit is available for a period of one year.

Definition of “Earned Income”

It is important to understand that a fellowship or grant type of payment is much different from income for services provided. Generally, a grant is not considered “earned income”. Grant recipients at the NIH are not considered to be providing services and, therefore, are not considered to be employees. This can make a difference in applying certain tax rules. The following tax rules apply to NIH Visiting Fellows (and other grant recipients who are not providing services):

- Moving expenses are not deductible. You must be an employee or self-employed to deduct moving expenses (other restrictions apply).
- Contributions to an IRA (individual retirement account) are not allowed unless you have “earned income”.
- The childcare credit is not allowed unless both working spouses have “earned income”. You must generally be filing as a resident alien to claim the childcare credit
- Fellowship grants are not considered “earned income” and are, therefore, not subject to social security and Medicare taxes.

INFORMATION SPECIFIC TO VISITING SCIENTISTS AND OTHER WAGE RECIPIENTS

How Income is Reported to Visiting Scientists

Employers and other payers of income are required to report the income that you have earned during the calendar year. One copy is provided to you; another copy is provided to the Internal Revenue Service. This is called the matching system. When you file your final tax report, the IRS will match the amount of income you have reported on your tax documents with the amount of income that the payer of the income has reported. Visiting Scientists and other wage recipients will receive **Form W-2** from the NIH by January 31 reporting the amount of wages received during the previous calendar year. The W-2 form should report all income paid to you from January 1 through December 1. Other forms that may be issued to you reporting income that you have earned include:

- Form 1099 Miscellaneous – Reports miscellaneous income paid to you during the calendar year. Some grantors report stipends paid on Form 1099 Miscellaneous.
- Form 1099 INT – Reports interest income paid to you during the calendar year.
- Form 1099 DIV – Reports dividend income paid to you during the calendar year.

A copy of Form W-2 is shown below:

A copy of Form W-2 is shown below:

a Control number		22222	Void	For Official Use Only ► OMB No. 1545-0008	
b Employer identification number				1 Wages, tips, other compensation	2 Federal income tax withheld
c Employer's name, address, and ZIP code				3 Social security wages	4 Social security tax withheld
				5 Medicare wages and tips	6 Medicare tax withheld
				7 Social security tips	8 Allocated tips
d Employee's social security number				9 Advance EIC payment	10 Dependent care benefits
e Employee's first name and initial		Last name		11 Nonqualified plans	12a See instructions for box 12
				13 Statutory employee Retirement plan Third-party sick pay	12b
				14 Other	12c
					12d
f Employee's address and ZIP code					
15 State Employer's state ID number		16 State wages, tips, etc.	17 State income tax	18 Local wages, tips, etc.	19 Local income tax
					20 Locality name

Form W-2 Wage and Tax Statement

Copy A For Social Security Administration — Send this entire page with Form W-2 to the Social Security Administration; photocopies are not acceptable.

2004
0000/1039

Department of the Treasury — Internal Revenue Service
For Privacy Act and Paperwork Reduction Act Notice, see separate instructions.

How Taxes Are Paid

Federal and state taxes must be paid throughout the year as you earn your income. The NIH is required to withhold federal and state taxes from each wage payment and deposit it with the US Treasury and the state of residence. The federal and state taxes withheld are not your actual tax liability. You will calculate your actual tax on your final tax Form 1040NR or Form 1040 at the end of the calendar year. Form W-2 will report the amount of tax that has been withheld during the year. You will report this amount on your final tax form as a payment. The NIH must follow certain rules in determining how much tax to withhold from your pay. If you are a wage recipient, you will be asked to complete Form W-4 for federal withholding. You must claim “single” and “1” on Form W-4. This determines how much tax NIH is required to withhold from your biweekly paycheck. You will also be asked to complete a withholding form for Maryland or your other state of residence.

If you have paid more taxes through withholding than your actual tax liability, you will receive a refund of the over withheld taxes after your final tax return is processed.

If you are entitled to a tax treaty benefit, you may be excused from federal tax withholding. You must submit Form 8233 to NIH to be claim exemption from federal withholding. Even if you are exempt from federal tax and withholding because of a treaty benefit, you must still file your final tax form at the end of the calendar year.

Moving Expenses

Moving expenses are deductible for individuals who are employees and move for a job-related reason. As an employee, you must move a distance of more than 50 miles, and you must work full-time for at least 39 weeks during the first twelve months of your move. If you work at the NIH as an employee, you may be allowed to deduct your moving expenses. Moving expenses are generally deducted in the year that the expenses are paid. Moving expenses include the transportation and storage of your household goods, and the cost of your transportation to your new place of employment. You can include the transportation cost (airfare) for any family member who was a member of your household at your prior residence. If you drive from your prior residence to your new residence, you can deduct the moving expense mileage rate of 15 cents per mile. You will need to keep receipts and records for all moving related expenses. Moving expenses are deductible as an adjustment to gross income. They are reported on Form 3903.

There are additional rules for self-employed individuals and there are special rules that apply if your employer has reimbursed you for moving expenses. See IRS Publication 521 for more information.

Tax Treaty Benefits for Visiting Scientists

Treaty benefits for Visiting Scientists and other wage recipients are included in the articles that apply to “Professors and Teachers”. These benefits are typically available for a period of two years from the date of arrival. In many cases, other restrictions apply. For example, the treaty will generally state whether or not the “Student/Trainee” article and the “Professor/Teacher” article can be used consecutively. In many treaties, the Professor/Teacher article can be used only once. The individual does not have to be a former or current professor or teacher; however, the treaty must state that the benefits are available for research performed for a public research institution. The treaty list on the next page includes the treaties that have benefits available to individuals performing research at a public, research institution. It is important to

understand that the IRS does not consider the NIH to be an educational institution. There are additional countries that have benefits for researchers performing research at an educational institution. These countries are not included in this list.

The following countries have tax treaty provisions available to individuals present in the U.S. for the purpose of performing research at a governmental research institution and receiving wages. These benefits are included in the Professor/Teacher articles of the treaties. See IRS Publication 901 for more information:

<u>Treaty Country</u>	<u>Eligibility From Article</u>	<u>Max. Amount Of Date of Arrival</u>	<u>Tax Exemption</u>
China The benefits for “Students/Trainees” (Art 20) and “Teacher/Researcher” cannot be used consecutively. Article 19 can be used only once for an aggregate time period of 3 years.	19	3 years	No Limit
CIS The cumulative benefits of the provisions for “Students/Trainees” and “Teacher/Researcher” cannot extend for a period of more than 5 years.	VI (1)	2 years	No Limit
Czech Republic The benefit of this article can be used only once and cannot be used consecutively with the “Student/Trainee” benefits.	21 (5)	2 years	No Limit
France The benefit of this article can be used only once; it can be used consecutively with the “Student/Trainee” article (Art 21), but both articles cannot be used for more than a total period of five years.	20	2 years	No Limit
Germany The benefits for “Students/Trainees” and “Teacher/Researcher” cannot be used consecutively. The individual cannot stay in the U.S. for longer than the 2-year period or all tax must be paid retroactively. This retroactive provision applies only to individuals claiming benefits under the Professor/Teacher category. It does not apply to the Student/Trainee provisions.	20 (1)	2 years	No Limit
Italy	20	2 years	No Limit
Portugal The benefit of this article can be used only once and cannot be used consecutively with the “Student/Trainee” benefits.	22	2 years	No Limit
Slovak Republic The benefit of this article can be used only once and cannot be used consecutively with the “Student/Trainee” benefits.	21 (5)	2 years	No Limit
Slovenia	20 (3)	2 years	No Limit
Venezuela	21 (3)	2 years	No Limit

Do not rely on this list as an interpretation of your individual eligibility to claim an exclusion from tax. In some situations it may be necessary to consult the treaty itself to determine if all qualifications are met.

H-1B Visa Holders

An H-1B visa holder will typically be present in the US working as an employee earning wages. The H-1B individual is not exempt from counting days for the IRS substantial presence test. The substantial presence test will be met in the first or second calendar year of presence depending upon the actual date of arrival and any other dates of US presence in the prior two years. If the substantial presence test is not met in the year of arrival, the individual may have the option of choosing to be taxed as a dual-status resident. A married dual-status alien also has the option of choosing to be taxed as a resident alien for the entire tax year. These choices are explained in detail in IRS Publication 519.

DEPARTING ALIENS - CERTIFICATE OF COMPLIANCE (“SAILING PERMIT”)

The Internal Revenue Service has issued regulations entitled “Certificates of Compliance with Income Tax Laws by Departing Aliens”. The regulations exempt alien students, industrial trainees, exchange visitors, and any spouse and children of those aliens, including those admitted on **F-1, F-2, J-1, J-2, H-3, and H-4** visas from the requirements to obtain a Certificate of Compliance (“Sailing Permit”) before departing the United States. Working spouses of program participants holding a J-2 visa are covered by the temporary regulations as long as their United States based income is in compliance with J-2 visa regulations. To qualify for the exemption, you must not have received any gross income from sources outside the United States while present in the United States, other than income permitted by the visa category. The exemption is available for either temporary or permanent departures.

The regulation specifically omits **H-1B** and **O** visa holders. Program participants at the NIH with an O visa or an H-1B visa will continue to require a Certificate of Compliance before departure from the United States. A Certificate of Compliance can be obtained from any IRS office. You can apply for a certificate of compliance by presenting Form 1040C in person at an IRS office approximately three weeks before your departure from the U.S. Form 1040C and instructions can be downloaded from the IRS website. Form 1040C is not a final tax report. You must still file Form 1040 or Form 1040NR at the end of the tax year.

MARYLAND STATE INCOME TAXES

In addition to the federal government, most of the states of the U.S. tax the income of their residents. In most cases, state income tax returns must be filed each year on or before April 15th (the same date that your federal income tax return is due). The following information pertains to facts important to filing a Maryland tax return:

- (1) Even though you may be a nonresident for federal tax purposes, it is likely that you will be considered a “resident” for Maryland tax purposes.
- (2) You must use the same filing status on your Maryland tax return as your federal tax return.
- (3) You are allowed the same number of personal exemptions on your state tax return as your federal tax return. For tax year 2004, the Maryland personal exemption amount is \$2,400.

- (4) All Maryland income tax filers are entitled to the standard deduction even if they must itemize on their federal tax return. However, you can **NEVER** itemize deductions **AND** take the standard deduction. Use the **ONE** method that gives you the larger deduction. The amount of your standard deduction depends upon your filing status. The worksheet below will help you calculate your Maryland standard deduction. Use the worksheet that corresponds with your *federal* filing status:

Single, Married Filing Separately

Married Filing Jointly, Head of Household

- If Maryland adjusted gross income is:

	<i>Standard</i>		<i>Standard</i>
\$1-10,000.....	\$1,500	<i>Deduction</i>	\$1-20,000.....\$2,000
			<i>Deduction</i>

- If Maryland adjusted gross income is between:

\$10,000 and 13,000	\$20,000 and 26,667
<i>Your Standard Deduction is 15% of Maryland Adjusted Gross Income</i>	

- If Maryland adjusted gross income is:

	<i>Standard</i>		<i>Standard</i>
Over \$13,000.....	\$2,000	<i>Deduction</i>	Over \$26,667.....\$4,000
			<i>Deduction</i>

- (5) If you itemize your deductions on federal Schedule A, you can claim the same itemized deductions from your federal tax return *except for the state taxes paid during the calendar year*.
- (6) If you itemize deductions on your federal tax return **and** you take a deduction for state taxes paid, **and** you receive a refund of part of these taxes in the following tax year, then this state tax refund is taxable for your *federal taxes* in the year in which you *receive* the refund. This refund is not taxable for your Maryland taxes.
- (7) Maryland does not recognize federal tax treaties. Therefore, even though your income may be excluded from taxation by the federal government, you must still file and pay Maryland taxes. Report tax treaty income as an addition to income on line 5, page 1, Form 502. Bank interest income is also taxable in Maryland.
- (8) If you are a part-year resident of Maryland, you must prorate your allowable deductions and exemptions according to your Maryland income factor. A Maryland income factor worksheet is provided in the Maryland tax booklet. If you are a part year resident who moved from a foreign country, your Maryland income factor will be **"1"**.
- (9) If your gross Maryland income is below a certain level (determined by your filing status), you may not be required to file and/or pay Maryland state income tax for that year. The minimum filing levels for 2004 are:
- | | |
|---------------------------|----------|
| Single | \$ 7,950 |
| Married (Joint Return) | 15,900 |
| Married (Separate Return) | 3,100 |
- (10) If you and your spouse both work and file a joint tax return, you may be entitled to an additional subtraction of up to \$1,200. See TWO-INCOME MARRIED COUPLE SUBTRACTION WORKSHEET in the Maryland tax booklet.
- (11) Maryland also assesses a local "piggyback" income tax. This tax is also calculated on the Maryland state tax return. The rate of local tax depends upon which county you live in. The local tax rate for Montgomery County for 2004 and 2005 is .032. Each county has a different tax rate.

2004 TAX RATE SCHEDULES

Single

If taxable income is:

\$0 to \$7,150
\$7,151 to \$29,050
\$29,051 to \$70,350
\$70,351 to \$146,750
\$146,751 to \$319,100
\$319,101.....

The tax is:

10%
\$715 + 15% of the amount over \$7,150
\$4,000 + 25% of the amount over \$29,050
\$14,325 + 28% of the amount over \$70,350
\$35,717 + 33% of the amount over \$146,750
\$92,592.50 plus 35% of the amount over \$319,100

Married Filing Jointly

If taxable income is:

\$0 to \$14,300
\$14,301 to \$58,100
\$58,101 to \$117,250
\$117,251 to \$178,650
\$178,651 to \$319,100
\$319,101.....

The tax is:

10%
\$1,430 + 15% of the amount over \$14,300
\$8,000 + 25% of the amount over \$58,100
\$22,787.50 + 28% of the amount over \$117,250
\$39,979.50 + 33% of the amount over \$178,650
\$86,328 + 35% of the amount over \$319,100

Married Filing Separately

If taxable income is:

\$0 to \$7,150
\$7,151 to \$29,050
\$29,051 to \$58,625
\$58,626 to \$89,325
\$89,326 to \$159,550
\$159,551.....

The tax is:

10%
\$715 + 15% of the amount over \$7,150
\$4,000 + 25% of the amount over \$29,050
\$11,393.75 + 28% of the amount over \$58,625
\$19,989.75 + 33% of the amount over \$89,325
\$43,164 + 35% of the amount over \$159,550

Head of Household

If taxable income is:

\$0 to \$10,200
\$10,201 to \$38,900
\$38,901 to \$100,500
\$100,501 to \$162,700
\$162,701 to \$319,100
\$319,101.....

The tax is:

10%
\$1,020 + 15% of the amount over \$10,200
\$5,325 + 25% of the amount over \$38,900
\$20,725 + 28% of the amount over \$100,500
\$38,141 + 33% of the amount over \$162,700
\$89,753 + 35% of the amount over \$319,100

MARYLAND TAX RATE SCHEDULE

<i>if your taxable income is at least</i>	<i>but not over</i>
\$0	\$1,000
\$1,000	\$2,000
\$2,000	\$3,000
\$3,000	

<i>Amount of tax</i>
2% of taxable income
\$ 20 + 3% of taxable income over \$ 1,000
\$ 50 + 4% of taxable income over \$ 2,000
\$ 90 + 4.75% of taxable income over \$ 3,000

County tax rates are assessed in addition to the state tax calculation shown here. County rates vary depending upon your county of residence.

